FILE COPY

FILED
JAN 18 1
CHARLES ELMORE

In the
Supreme Court of the United States

OCTOBER TERM, 1929

No. 301

RAILROAD COMMISSION OF WISCONSIN, LEWIS E. GETTLE, ADOLPH KANNEBERG, et al., Etc.,

Defendants and Appellants,

v.

W. G. MAXCY, as Receiver of the Washburn Water Works Company, and Washburn Water Works Company,

Plaintiffs and Respondents.

RESPONDENTS' BRIEF

H. L. BUTLER,
H. H. THOMAS,
B. H. STEBBINS,
R. M. STROUD,
R. M. RIESER,
Attorneys for Plaintiffs and Respondents.

OLIN AND BUTLER,
Of Counsel.

Straus Printing Co., Madison, Wis.

INDEX

Page No.

Statement of Facts 2

The value claimed before the Commission..... 2

The order of the Commission..... 3

The Evidence Before the Commission..... 3

The Commission Used a Split Inventory Valuation Never Offered in Evidence..... 4

Effect of Commission's Consideration of Case..... 5

The Commission Changed its Method of Computing Depreciation 6

The Actual Operating Expenses of the Company Were Not Used by the Commission..... 7

The Actual Present Value of the Plaintiff's Property.. 10

Cause of Difference Between Plaintiffs' and Defendants' Experts 12

The Rate Base Established by Plaintiffs..... 12

Summary of Argument 15

Argument 19

The Commission without other than evidence of the cost of reproduction before it has disregarded such evidence and has made an arbitrary valuation of the

Page No.

property of the company without any evidence to support the same thereby confiscating the company's property 19

A. It attempted to sustain this arbitrary result on asserted economic conditions in Washburn, which are speculative and wholly unrelated to the plaintiff's property 19

1. The plaintiffs' own business history establishes the Commission's action as arbitrary..... 19

2. The plant of the plaintiffs is not too large for the community 19

3. The claim of decrease in population is unsupported in the record 20

4. The asserted tax delinquency does not justify the conclusions of the Commission drawn therefrom 21

5. The financial condition of the City of Washburn shows that the city is above the average..... 23

6. The Commission under the decisions of the state and federal courts was required to give consideration to and have its valuation reflect such consideration of the increased cost of reproducing the property at present day prices. 23

B. The valuation alleged by the Commission to reflect the cost of reproduction as of the time of its decision was in fact inadequate..... 24

Page No.

1. The valuation thus submitted by the Commission's engineers being of a date eleven months preceding the actual decision, during which time a material change in prices took place, and since the prices on the date of this decision more nearly reflected the average prices during a considerable period preceding the valuation, the valuation figures adopted were inadequate 24

2. One reason for the low cost of reproduction valuation submitted by the Commission's engineers is the unjustifiable depreciation of the property 25

C. The Commission under the decisions of the state and federal courts was required to give consideration to and have its valuation reflect such consideration of the increased cost of reproducing the property at present day prices.... 26

D. By not allowing going value and failing to fix that element of value in this case the Commission deprives the plaintiffs of an element of value and therefore of a property right..... 30

E. The plaintiffs are entitled to the "independent judgment of the court as to both the law and the fact" especially where it is apparent from the proceedings that a deliberate attempt on the part of the Commission is being made to circumvent the decisions of this court guaranteeing due process 31

Page No.

F. The Commission's only justification for ignoring the decisions of the courts are the conditions referred to above but the record fails to disclose any justification for such action and nowhere in the evidence is it shown that the conditions relied upon by the Commission had any effect upon the value of the property of the plaintiffs 32

G. The efforts on the part of the Commission to find a value by comparing rates in Washburn with rates in other communities and the claim that the rates in Washburn were unusually high and that this fact affected the value of the property were clearly erroneous..... 35

The Commission has ignored actual operating expenses and substituted its own estimate of what should be proper operating expenses, thereby decreasing the allowance for expenses of the company by over $5,000 without any evidence to support such action..... 36

A. The reduction of actual pumping costs by $1,650 annually was arbitrary 36

B. The reduction of distribution, commercial and general expenses below the actual previous amounts for such items was purely arbitrary. 43

C. The failure to allow amortization of accumulated legal expense and receiver's fees was wholly arbitrary 43

D. By thus substituting a theory of operating ex-

Page No.

penses over $5,000 less than the actual operating expenses the Commission improperly and illegally interfered with the management of the company and the result thus obtained can therefore not be sustained 44

Upon either objection raised by the record the order of the Commission must fall 46

TABLE OF CASES

Page No

Ashland Water Co. vs. Railroad Comm., 7 Fed. (2nd) 924, 929, 930, 935, 936, 937 ..... 4, 27, 33, 3

Bluefield Waterworks & Improvement Co. vs. Public Service Comm., 262 U. S. 679 ..... 27, 3

Brush Electric Co. vs. Galveston, 262 U. S. 443 2

Columbus Gas & Fuel Company vs. Columbus, 17 Fed. (2nd) 630 at 640 4

Consolidated Gas Co. vs. Prendergast, 6 Fed. (2nd) 243 at 280 2

Consolidated Gas Co. vs. Newton, 267 Fed. 231 at 236-238 2

Georgia Railway & Power Co. vs. Railroad Comm., 262 U. S. 625 2

Joplin Gas Co. vs. Public Service Comm., 296 Fed. 271, 277 2

McCardle vs. Indianapolis Water Co., 272 U. S. 400 2

Minneapolis vs. Rand, 285 Fed. 818, 826, 827, 830 ..... 27, 3

Minneapolis, St. P. & Ste. M. R. R. vs. Railroad Commission, 136 Wis. 146, 164 4

Mobile Gas Co. vs. Michigan Public Utilities Comm., 292 Fed. 139, 143 2

Monroe Gas Light Co. vs. Michigan Public Utilities Comm., 11 Fed. (2nd) 319, 325 4

New York Telephone Co. vs. Prendergast, 300 Fed. 822 .. 2

Ohio Utilities Co. vs. Public Utilities Comm. of Ohio, 267 U. S. 359, 362, 363 ..... 27, 28, 30, 4

Page No.

Ohio Valley Water Co. vs. Ben Avon, 253 U. S. 287, 289. 32

Patterson vs. Mobile Gas Co., 293 Fed. 208..... 45

Public Service Railway Co. vs. Board of Public Utility Commissioners, 276 Fed. 979 at 987..... 30

San Diego Water Works Co. vs. San Diego, 50 Pac. 633; 118 Cal. 556, 574 45

Southwestern Bell Telephone Co. vs. City of Ft. Smith, 294 Fed. 102, 103, 106, 108.....30, 45

Spring Valley Water Works vs. San Francisco, 192 Fed. 137, 190 45

St. Joseph R. L. H. & P. vs. Public Service Comm., 268 Fed. 267, 268 (W. D. Mo. 1920)..... 45

St. Louis & O'Fallon R. Co. vs. U. S., 279 U. S. 461, 486.. 28

Standard Oil Co. vs. Southern Pacific Co., 268 U. S. 146 27

State ex rel. Southern Bell Telephone Co. vs. Public Service Comm., 262 U. S. 276, 288, 289 (1923).....27, 44

State vs. Washburn Water Works Company, 182 Wis. 287 22

Van Wert Gas Light Co. vs. Michigan Public Utilities Comm., 299 Fed. 670 at 673..... 27

Waukesha Gas & Electric Co. vs. Railroad Comm., 191 Wis. 565 at 569 .....25, 26

Winona W. M. L. & P. Co., 276 Fed. 996..... 45

Wisconsin-Minnesota Light & Power Co. vs. Railroad Comm., 183 Wis. 96, 103, 104, 105.....33, 45

In the
Supreme Court of the United States
OCTOBER TERM, 1929
No. 301

RAILROAD COMMISSION OF WISCONSIN, LEWIS E. GETTLE, ADOLPH KANNEBERG, et al., Etc.,

Defendants and Appellants,

v.

W. G. MAXCY, as Receiver of the Washburn Water Works Company, and Washburn Water Works Company,

Plaintiffs and Respondents.

RESPONDENTS' BRIEF

This is an appeal from a judgment and decree of the District Court of the United States for the Western District of Wisconsin, three judges sitting as a statutory court, entered April 5, 1929 enjoining the appellants from interfering with the respondents in charging and collecting reasonable rates for water furnished to the City of Washburn, Wisconsin, and from enforcing an order of the Railroad Commission of Wisconsin dated December 4, 1928, prescribing certain rates for water furnished in said city.

The case is founded upon two principal claims based upon facts alleged in the complaint and admitted in the answer:

First: The Commission has ignored actual operating expenses and substituted its own estimate of what should be proper operating expenses, thereby decreasing the allowance for expenses of the company by over $5,000 without any evidence to support such action.

Second: The Commission without other than evidence of the cost of reproduction before it has disregarded such evidence and has made an arbitrary valuation of the property of the company without any evidence to support the same thereby confiscating the company's property.

STATEMENT OF FACTS

The value claimed before the Commission:

The plaintiffs filed with the Commission in December, 1927, a schedule of increased rates, a copy of which is attached to the complaint as Exhibit B, (R. 31-38) in which it was claimed, as it was claimed in the proceeding before the Commission that the property devoted to the public use was of the value of One Hundred and Thirty Thousand ($130,000.00) Dollars, and that the revenue of the company was insufficient to yield a fair return.

The Commission, contrary to the provisions of Sec. 196.20 Wisconsin Statutes 1927, refused to accept this rate for filing. This statute reads as follows:

"No change shall thereafter (after the passage of the Wisconsin Utility Act) be made in any schedule, including schedules of joint rates, except upon ten days' notice to the commission, and all such changes shall be plainly indicated upon existing schedules, or by filing new schedules in lieu

thereof ten days prior to the time the same are to take effect; provided, that the commission, upon application of any public utility, may prescribe a less time within which a reduction may be made."

The company, thereupon expressly reserving its rights under such original filing, made application for such increase in rates.

The Order of the Commission:

Following the hearing upon this application and on December 4, 1928, eleven months after the date used for pricing the property of the plaintiffs, the Commission issued an order (Exhibit C, R. 38-42) establishing the value of the property of the plaintiffs at Seventy-Five Thousand ($75,000) Dollars against the claimed value of One Hundred Thirty Thousand ($130,000) Dollars.

The Evidence Before the Commission:

In arriving at this value or rate base the Commission had before it as the lowest competent estimate of value the valuation of its own engineering department fixing the cost of reproducing the physical property without working capital, going value and material and supplies at One Hundred Fourteen Thousand Eighty-Nine ($114,089) Dollars and depreciated at Eighty-Seven Thousand One Hundred Sixteen ($87,116) Dollars. (Exhibit C. R. 39).

This valuation was made as of January 1, 1928 and had the Commission used the prices for the physical elements composing the plant of the plaintiffs prevailing at or about the date of its decision, the cost of reproduction would have been One Hundred Twenty-One Thousand Six Hundred Seventeen ($121,617) Dollars and depreciated Ninety-Three Thousand Three Hundred Sixty-Four ($93,364) Dollars for the same

items. (R. 57). Such valuation would have more nearly reflected price levels for a period of several years preceding the valuation. (R. 101, R. 85, R. 86).

Likewise the Commission had before it an appraisal as of June 30, 1923 showing a value undepreciated of One Hundred Thirty-Two Thousand Eight Hundred Sixty-Two ($132,862) Dollars. In arriving at this value the Commission had added but 12% for general overhead as against 15% now recognized by the Commission as being proper so that had this 12% item been increased to 15% in accordance with the present practice of the Commission the total value would have been One Hundred Thirty-Six Thousand Four Hundred Twenty-One ($136,421) Dollars.

The Commission Used a Split Inventory Valuation Never Offered in Evidence:

In addition the Commission referred to a split inventory valuation of Seventy-One Thousand Five Hundred Thirty ($71,530) Dollars which was not introduced at the hearing before the Commission or in the trial court, but this value was slightly over Thirty-Five Hundred ($3,500) Dollars less than the figure it finally adopted as the value of the property. A split inventory valuation takes the ten year average cost of reproducing property actually installed prior to January 1, 1916 at such average cost and adds actual costs of elements installed after January 1, 1916 and then depreciates the same. (See *Ashland Water Company vs. Railroad Commission*, 7 Fed. (2nd), 924, 929, 930.)

The split inventory figure of Seventy-One Thousand Five Hundred Thirty ($71,530) Dollars referred to by the Commission however could not have included One Thousand ($1,000) Dollars of additions made between the date of the hearing before the Commission and the decision by the Com-

mission December 4, 1928. (See Hartt affidavit, R. 86, Maxcy affidavit R. 77.)

Nor could it have included any allowance for working capital or materials and supplies. Items which the Commission estimated in 1925 would require an additional Three Thousand ($3,000) Dollars although in this proceeding it reduced that figure to Twenty-Five Hundred ($2,500) Dollars. If these items were considered it does not appear so of record and the Commission nowhere has indicated that they were considered. However, these items if added to the asserted split inventory valuation so as to have brought that valuation to the date of the Commission's inquiry and so as to have reflected the various elements considered by the Commission would have produced a total split inventory value of Seventy-Five Thousand Five Hundred Thirty ($75,530) Dollars or Five Hundred Thirty ($530) Dollars more than was allowed by the Commission in this case and that without any allowance for going value.

Effect of Commission's Consideration of Case:

It may be fairly stated therefore that while the Commission went through the motion of considering a valuation reflecting the cost of reproduction as presented to it by its own staff, its ultimate conclusion and decision was based upon an arbitrary split inventory valuation never introduced into the record.

The force of this action by the Commission is emphasized by the allegations of the complaint admitted in the answer to the effect that if to the cost of reproducing the property, found by the Commission in 1910, there is added the actual additions at actual cost to the date of this inquiry, the total value thus arrived at is Eighty-Six Thousand ($86,000.00) Dollars. The 1910 valuation, reflecting as it would substantially the prices up to 1916, with additions at actual cost after

that time, is substantially a split inventory valuation. (Maxcy affidavit, R. 77.)

The Commission Changed its Method of Computing Depreciation:

The record also shows that the Commission changed its policy with respect to depreciation between 1923 and 1928. A comparison of the figures used by the Commission's engineers demonstrates this. (R. 86).

In the 1923 valuation the property was determined to be in 85.7 per cent condition. (R. 82). At that time the majority of the property had been in place thirty-six years.

In the 1928 decision of the Commission five years after the former valuation, the property was found to be in 76 per cent condition. In other words the Commission for thirty-six years depreciated the property 14.3 per cent and for five years following the thirty-six year period depreciated it 9 per cent. (R. 82).

If the Commission had used the same rate of depreciation for the thirty-six year period that it used for the five year period following 1923, the property in 1923 would have been in 20.5 per cent condition and in 13.5 per cent condition in 1928. On the other hand, if the Commission had followed its previous practice of depreciating the property, then at the time of its decision the property would have suffered an additional 2.7 per cent depreciation, or would have been in 83 per cent condition, as against the 76 per cent assigned to it by the Commission's engineers.

The reason for this change in this case was not explained by the Commission, either in its decision or by any evidence that was offered.

An examination of the Commission's figures indicates, however, that this higher rate of depreciation employed by the

Commission is due to a change made from the four per cent sinking fund method of computing depreciation to the straight line method of depreciation. This change in procedure is contrary to the accepted practice of the industry and for that reason is arbitrary. (Hartt affidavit R. 85).

The Actual Operating Expenses of the Company Were Not Used by the Commission:

The Commission also had before it the operating expense of the company for the five-year period preceding 1927, averaging Fifteen Thousand Three Hundred Two and 49/100 ($15,302.49) Dollars per year, (R. 32, 78) and in addition the 1927 operating expenses also before the Commission show that the actual operating expenses of this plant cannot be reduced below the average of Fifteen Thousand Three Hundred Two and 49/100 ($15,302.49) Dollars per year as reflected by the history of the preceding six year period. For 1927 they were Fifteen Thousand Fifty-five and 52/100 ($15,055.52) Dollars and for 1928, Fourteen Thousand Nine Hundred Thirteen and 19/100 ($14,913.19) Dollars; all these items being before any allowance for depreciation was made.

Adding thereto adequate allowance for depreciation or Eleven Hundred Forty-One and 81/100 ($1,141.81) Dollars, or 1 per cent on the cost of reproduction found by the Commission as of January 1, 1928, and One Thousand ($1,000) Dollars, annually to amortize the Railroad Commission and legal expenses now accumulated and unpaid (R. 78), the actual operating expenses will be Seventeen Thousand Fifty-Four and 90/100 ($17,054.90) Dollars before any return will be forthcoming. (Complaint R. 14-15 admitted by answer R. 60, last paragraph, Maxcy affidavit page 78, R. 93.) It should be noted that the six year average of operating ex-

penses above does not take into consideration an adequate reservation for additional taxes, resulting from a higher valuation placed upon the property by the City of Washburn after 1926, the valuation having been increased from Fifty Thousand ($50,000.00) Dollars to Seventy-Five Thousand ($75,000.00) Dollars.

These figures represent disbursements that will actually be made based on the experience of the seven years 1922-1928 inclusive, and as filed in the annual returns of the company do not include obligations incurred for legal fees, nor compensation for the receiver, which, according to the allegations of the complaint, would bring the operating expenses of this company up to Eighteen Thousand ($18,000.00) Dollars per year (Complaint R. 14-15 admitted by Answer R. 60, Paragraph XIV, Last two sentences), or using the higher valuations shown in the proceeding, the total revenue required before return on the value of the property, would be Nineteen Thousand Two Hundred and Fifty-Four ($19,254.00) Dollars. (Maxcy affidavit R. 78 and 80).

Against this total expense the company has actual revenue, averaging Seventeen Thousand and Seventy ($17,070.00) Dollars, during the five-year period aforesaid, and for 1927 Seventeen Thousand Nine Hundred Ninety-Six and 24/100 ($17,996.24) Dollars, and Seventeen Thousand Six Hundred Thirty-Nine and 15/100 ($17,639.15) Dollars for the year 1928.

Against this actual operating history of this company, the Commission assumed a hypothetical operating estimate, with operating expenses at Twelve Thousand Eight Hundred and Sixty-Seven ($12,867.00) Dollars per year for all items except return upon investment, *or over five thousand ($5,000) Dollars less than the actual operating expenses.* To do this the Commission cut down the actual pumping expenses by Sixteen Hundred and Fifty ($1,650.00) Dollars. This cut

was made because, as the Commission in its order states (Exhibit C), (R. 40-41) the pumping cost could be reduced by installing a smaller pump and thereby obtaining lower rates for electrical energy purchased. The contention is denied and Mr. Maxcy outlines the care taken in selecting the present pump. (Maxcy affidavit R. 79). Moreover the present power contract would prevent such saving. (Maxcy affidavit R. 79).

The Commission says "in order to secure the lower rate for power the large motor and pump must be idle *and with intelligent operation and fortunate distribution of large fires or other necessity of operating the large pump a substantial saving may be made.* The margin appears to be sufficient to write off the fixed charges and the cost of additional equipment and labor of installation within a few years, assuming occasional use of the large pump and motor now installed *with wise handling, proper installation and co-operation and favorable circumstances the saving may* amount to two thousand dollars a year." (R. 40). Note that the action of the commission is based upon pure speculation.

This conclusion was arrived at in spite of the fact that its engineers on the hearing testified (admitted by answer, R. 57) that they had insufficient evidence to recommend the installation of an additional pump and the answer admits this to be true. (R. 57).

Without any evidence whatsoever in the record, the Commission cut the distribution expense, commercial and general expense in the amount of Twenty-seven hundred eighteen and 45/100 ($2718.45) Dollars below those items representing actual expenditures for 1927. (See admission in answer R. 57). In other words, the Commission, without any evidence in the record made an arbitrary reduction in its estimate of operating expenses of Forty Three Hundred Sixty Nine and 28/100 ($4369.28) Dollars. (R. 57).

While the answer alleges that the accounts of the plaintiff were not kept in accordance with the uniform classification of accounts, the immateriality of this fact is reflected by the correction of the accounts made by the Commission's auditors. The resulting variation made a difference of only Fifty ($50.00) Dollars.

Also the Commission excluded from its estimate of operating expenses the actual obligations of the company for receiver's fees and legal expenses, claiming that it was not going to allow anything for expenses "incurred fighting this Commission's orders." (R. 41).

The complaint alleges and the answer admits that not all of the legal expenses were incurred in fighting the Commission's orders and that every suit commenced by the company to fight the Commission's orders was successful. (R. 57).

By this method of cutting the estimated operating expenses by Forty Three Hundred Sixty Nine and 28/100 ($4369.28) Dollars below those actually representing the operating expenses in 1927, and by disallowing accrued charges for Railroad Commission and legal and receiver's expense, amounting to One Thousand ($1,000.00) Dollars, annually, the Commission provided a return of Fifty Two Hundred and Fifty ($5250.00) Dollars, or seven per cent on the Seventy Five Thousand ($75,000.00) Dollars of value, which it assigned to this plant.

The Actual Present Value of the Plaintiff's Property:

While the foregoing figures as to value of the property, have been presented for the purpose of showing that the Commission arrived at an arbitrary result and thereafter the figures were used in comparison with the Commission's valuation of Seventy Five Thousand ($75,000.00) Dollars, the evidence now submitted shows that the depreciated value of

the physical property, with materials and supplies and working capital was One Hundred Seventeen Thousand Nine Hundred and Fifty Two ($117,952.00) Dollars and with going value One Hundred Twenty Two Thousand Nine Hundred and Fifty Two ($122,952.00) Dollars. Hartt affidavit R. 84).

Had the Commission used the prevailing prices at the time of announcing its decision, nearly a year after hearing the testimony (December, 1928, or January 1, 1929, instead of January 1, 1928), and had the Commission taken only the information of its own engineer, and incidentally the lowest figure of value submitted and brought it down to the date of the Commission's order to reflect the increase in cost of reproduction, resulting from the recovery of a temporary slump, the Commission's own engineer would have shown a value for this property of One Hundred Twenty One Thousand Six Hundred and Seventeen ($121,617.00) Dollars against his original One Hundred Fourteen Thousand and Eighty Nine ($114,089.00) Dollars. (Hartt affidavit R. 86-87, Thiesen R. 97). Moreover this item of One Hundred Twenty One Thousand Six Hundred and Seventeen ($121,617.00) Dollars, the undepreciated reproduction cost of the property, after bringing the Thiesen valuation down to date, the date of the Commission's order, was about ten per cent under that of Hartt, representing the company in this case. (Hartt affidavit R. 86). While as a result of applying excessive and arbitrary depreciation methods, the depreciated value of the property was 22 per cent less under the Thiesen valuation than it was under the Hartt valuation. (Hartt affidavit R. 87). The table of comparisons in the record illustrates this situation graphically. (R. 87).

Cause of Difference Between Plaintiffs' and Defendants' Experts:

That this difference between the expert for the Commission and the expert for the company is due primarily to the change in the method of determining the proper depreciation by the Commission is demonstrated by applying instead of the 76 per cent figure found by Thiesen, as representing the average condition of this property in 1928, the 83 per cent figure which would reflect the depreciation of this property had the depreciation ascribed in 1923 been carried down to date. Multiplying therefore the corrected Thiesen valuation of One Hundred Twenty One Thousand Six Hundred and Seventeen ($121,617.00) Dollars by 83 per cent and the result is One Hundred Two Thousand ($102,000.00) Dollars, which would represent Thiesen's depreciated value of the physical property of the plant as of the time the Commission made its decision in 1928 and after applying a rate of depreciation comparable with the depreciation assigned to the property in 1924.

The Rate Base Established by Plaintiffs:

On this basis again there would be a difference between Hartt, representing the plaintiffs, and Thiesen, representing the Commission of less than 13 per cent. Adding to the One Hundred and Two Thousand ($102,000.00) Dollars item, a proper allowance for working capital, materials and supplies of Three Thousand ($3,000.00) Dollars, as found in 1925 by the Commission and an additional One Thousand ($1,000.00) Dollars, for additions made and not included in the Thiesen valuation, plus Five Thousand ($5,000.00) Dollars, as going value, and the depreciated value of this property with working capital, materials and supplies and going value, corrected to reflect the judgment of the Commission, on the basis of the

1924 valuation, is One Hundred and Eleven Thousand ($111,000.00) Dollars, or One Thousand ($1,000.00) Dollars more than the basis upon which the present temporary rates were established, and but Eleven Thousand ($11,000.00) Dollars less than that set forth in the valuation submitted by Mr. Hartt for the company.

Bearing in mind that on the present rates, the annual revenue provided bythe temporary rate schedule proposed in this proceeding (Exhibit D, R. 42-45), will produce not to exceed Twenty-seven Thousand Nine Hundred and Fifty Eight ($27,958.00) Dollars, (R. 45) the rates now in force will be inadequate to yield a fair return on even One Hundred and Ten Thousand ($110,000.00) Dollars valuation. The later check of Mr. Meuwsen (R. 88) shows that even less than was originally estimated will be realized in that the expected revenue will not exceed Twenty Seven Thousand Two Hundred and Eighty One ($27,281.00) Dollars, against the required revenue on the One Hundred and Twenty Two Thousand ($122,000.00) Dollars valuation of Twenty Nine Thousand and Ninety ($29,090.00) Dollars, (Maxcy affidavit, R. 47) this will be Eighteen Hundred and Nine ($1809.00) Dollars short of the required amount. A 7 per cent return would require Twenty Seven Thousand Six Hundred and Ninety Four ($27,694.00) Dollars in revenue, which would be Four Hundred and Thirteen ($413.00) Dollars, more than will be realized on the present rates. A 6 per cent return would require Twenty Six Thousand Five Hundred and Seventy Four ($26,574.00) Dollars, or Seven Hundred and Seven ($707.00) Dollars less than the amount to be realized on the present rates. If on the other hand we check the present rates on the basis of One Hundred and Ten Thousand ($110,000.00) Dollars valuation, being that assumed for the temporary rates, we would reduce the basis Three Hundred and Fifty Eight ($358.00) Dollars annually and would require in annual

revenues Twenty Seven Thousand Six Hundred and Ninety Six ($27,696.00) Dollars to obtain an 8 per cent return, as against Twenty Seven Thousand Two Hundred and Eighty One ($27,281.00) Dollars, to be realized on the present rates, that is Four Hundred and Fifteen ($415.00) Dollars more than will be realized, while a 7 per cent return would require annual revenues of Twenty Six Thousand Five Hundred and Ninety Six ($26,596.00) Dollars, or Six Hundred and Eighty Five ($685.00) Dollars less than the anticipated results under the present rates.

SUMMARY OF ARGUMENT

The order of the Commission is attacked on two propositions that appear undisputed in the record:

FIRST: THE COMMISSION HAS IGNORED ACTUAL OPERATING EXPENSES AND SUBSTITUTED ITS OWN ESTIMATE OF WHAT SHOULD BE PROPER OPERATING EXPENSES, THEREBY DECREASING THE ALLOWANCE FOR EXPENSES OF THE COMPANY BY OVER $5,000 WITHOUT ANY EVIDENCE TO SUPPORT SUCH ACTION.

SECOND: THE COMMISSION WITHOUT OTHER THAN EVIDENCE OF THE COST OF REPRODUCTION BEFORE IT HAS DISREGARDED SUCH EVIDENCE AND HAS MADE AN ARBITRARY VALUATION OF THE PROPERTY OF THE COMPANY WITHOUT ANY EVIDENCE TO SUPPORT THE SAME THEREBY CONFISCATING THE COMPANY'S PROPERTY.

The foregoing propositions are not contradicted but it is claimed by counsel that they are justified because of peculiar conditions alleged to exist in Washburn.

The Commission without other than evidence of the cost of reproduction before it has disregarded such evidence and has made an arbitrary valuation of the property of the company without any evidence to support the same thereby confiscating the company's property.

A. It attempted to sustain this arbitrary result on asserted economic conditions in Washburn which are speculative and wholly unrelated to the plaintiff's property.

1. The plaintiff's own business history establishes the Commission's action as arbitrary.

2. The plant of the plaintiffs is not too large for the community.

3. The claim of decrease in population is unsupported in the record.

4. The asserted tax delinquency does not justify the conclusions of the Commission drawn therefrom.

5. The financial condition of the City of Washburn shows that the city is above the average.

6. The Commission under the decisions of the state and federal courts was required to give consideration to and have its valuation reflect such consideration of the increased cost of reproducing the property at present day prices.

B. The valuation alleged by the Commission to reflect the cost of reproduction as of the time of its decision was in fact inadequate.

1. The valuation thus submitted by the Commission's engineers being of a date eleven months preceding the actual decision, during which time a material change in prices took place, and since the prices on the date of this decision more nearly reflected the average prices during a considerable period preceding the valuation, the valuation figures adopted were inadequate.

2. One reason for the low cost of reproduction valuation submitted by the Commission's engineers results from unjustifiable depreciation of the property. This is demonstrated by a reading of the analysis in the statement of facts herewith. The appellants' counsel seeks to justify it however and in doing so misconstrues the effect of the testimony.

C. The Commission under the decisions of the state and federal courts was required to give consideration to and have

its valuation reflect such consideration of the increased cost of reproducing the property at present day prices.

D. By not allowing going value and failing to fix that element of value in this case the Commission deprives the plaintiffs of an element of value and therefore of a property right.

E. The plaintiffs are entitled to the "independent judgment of the court as to both the law and the fact" especially where it is apparent from the proceedings that a deliberate attempt on the part of the Commission is being made to circumvent the decisions of this court guaranteeing due process.

F. The Commission's only justification for ignoring the decisions of the court are the conditions referred to above but the record fails to disclose any justification for such action and nowhere in the evidence is it shown that the conditions relied upon by the Commission had any effect upon the value of the property of the plaintiffs.

G. The efforts on the part of the Commission to find a value by comparing rates in Washburn with rates in other communities and the claim that the rates in Washburn were unusually high and that this fact affected the value of the property were clearly erroneous.

The commission has ignored actual operating expenses and substituted its own estimate of what should be proper operating expenses, thereby decreasing the allowance for expenses of the company by over $5,000 without any evidence to support such action.

A. The reduction of actual pumping costs by $1,650 annually was arbitrary.

B. The reduction of distribution, commercial and general expenses below the actual previous amounts for such items was purely arbitrary.

C. The failure to allow amortization of accumulated legal expense and receiver's fees was wholly arbitrary.

D. By thus substituting a theory of operating expenses over $5,000 less than the actual operating expenses the Commission improperly and illegally interfered with the management of the company and the result thus obtained can therefore not be sustained.

Upon either objection raised by the record the order of the Commission must fall.

ARGUMENT

THE COMMISSION WITHOUT OTHER THAN EVIDENCE OF THE COST OF REPRODUCTION BEFORE IT HAS DISREGARDED SUCH EVIDENCE AND HAS MADE AN ARBITRARY VALUATION OF THE PROPERTY OF THE COMPANY WITHOUT ANY EVIDENCE TO SUPPORT THE SAME THEREBY CONFISCATING THE COMPANY'S PROPERTY.

A. It attempted to sustain this arbitrary result on asserted economic conditions in Washburn which are speculative and wholly unrelated to the plaintiff's property.

1. The plaintiffs' own business history establishes the Commission's action as arbitrary.

The Commission has entirely misconceived the conditions in the city of Washburn. The company at the end of 1928 had 135 more customers than it had in 1914 and but 85 customers less than during the brightest days of the war boom. Thus the company has shown marked improvement over conditions existing in 1914, in that it has far more customers than it had at that time. In fact it shows an increase of 27 per cent in net customers between 1914 and 1928.

2. The plant of the plantiffs is not too large for the community.

To sustain the claim that the plant is over-built counsel refers to certain pictures taken in Washburn, but these do not demonstrate anything. The pictures are only another effort to overstate the situation in Washburn.

Counsel apologizes for this argument in the next breath by saying "We do not contend that the construction of the plant

was wasteful, extravagant or imprudent." (Brief, page 37.) And again says "We confess that no exhaustive study was made by the Commission or by counsel representing the appellant to show the extent of over-development of the utility property." (Brief, page 37). The answer of the defendants (R. 62-63) says

> "Defendants admit that the plaintiffs' plant was and is well designed and constructed, that certain hydrants of which complaint was made were installed under direction of the city officials, and that there was no lack of reasonable or proper prudence in design or construction."

3. The claim of decrease in population is unsupported in the record.

That the war population was temporary and did not affect or require any extensive investment by the plaintiffs is evidenced by the fact that it resulted in but a small increase of water customers. The removal of the powder company houses (R. 91) is further evidence of that fact.

The only authentic evidence of the population at the time of the trial was the census of 1920, showing 3707 people in Washburn.

The remaining evidence illustrates the length to which the appellants are driven to justify their position. Evidence of the ministers of the decline of church population of two congregations may be, as suggested at the argument in the lower court, accounted for as well by poor preaching as on any theory of depopulation. Decline in church population everywhere has progressed to the point where it presents a crisis in the church world. Many reasons for it have been advanced, including the automobile, prohibition and the radio, but we venture to say that the theory of counsel in this case is unique in claiming that this fact can be connected with anything affecting a water utility. The fact remains that those congre-

gations wherever situated having good preachers are growing and the rest are declining.

The only other evidence, that there are now only 2700 people in Washburn, as asserted in appellants' brief, is based upon the affidavit of W. A. Robinson, a newspaper editor who says he made a check of potential newspaper customers in said city and "derived at the conclusion, and is of the opinion that the population of said city was about 2700" at the time of the affidavit. (R. 110).

4. The asserted tax delinquency does not justify the conclusions of the Commission drawn therefrom.

Tax delinquency is cited as another evidence of adverse conditions in Washburn, but nowhere in the record is it shown that a single lot, subject to delinquent taxes, is occupied by improvements or that a single delinquent lot is responsible for a single cent of investment by the plaintiff company.

How then can that situation benefit the appellants? A town which has had a water works company since 1889, has been a county seat since that time, shows a steady increase in customers of its water utility, an increase in assessed and true valuation over that preceding the war boom, demonstrates its stability when during a boom period prices nearly doubled and yet the recession following the war has never gone below the level preceding the boom. That a sudden increase in the population undoubtedly resulted in speculation, that as a result of such speculation additional platting was done, and that at the end of the boom these artificial conditions were destroyed, is to be expected and the delinquent tax situation only reflects that situation. Washburn is to be credited with unusual stability to have resisted the reaction during the ten-year period following the boom by showing that artificial values have been only partially wiped out. The

management of the company with years of experience (R. 45) demonstrated its competency by avoiding over-expansion on its part during this temporary period and by resisting demands on the part of the appellant Commission to force such over-expansion.

State vs. Washburn Water Works Company, 182 Wis. 287.

While a considerable effort is made in the appellants' brief to picture a progressive retrogression in Washburn, a claim which the record does not justify, in our judgment, it is true of course that Washburn enjoyed a temporary boom. However, this was never reflected by any demands of the plaintiffs, the rates remained unchanged from 1910 to 1921, and the increase in 1921 was founded upon increased operating expenses and not because asserted increase in value claimed to be due to the temporary war boom, as reflected by the larger employment at the Du Pont Powder factory. While values mounted from one million, two hundred forty one thousand two hundred and twenty three ($1,241,223) Dollars in 1914, at the out-break of the war, to two million six hundred nine thousand six hundred and sixty eight ($2,609,668) Dollars right after the war on all property within the city of Washburn, and then declined to one million three hundred forty two thousand four hundred and eighty ($1,342,480) Dollars by 1928 (R. 113-114), the plaintiff company did not attempt to capitalize this value. On the other hand the Commission attempted unsuccessfully in its 1924 value to take this decrease in temporary value and apply it against the company. (R. 7, 59). It is a fact that values today in Washburn are one hundred thousand ($100,000) Dollars higher than they were in 1914. (R. 113, 114). And that this condition exists in spite of the fact that over one hundred houses, erected dur-

ing the temporary war period, have been removed and many others have been destroyed by fire. (R. 91).

5. The financial condition of the City of Washburn shows that the city is above the average.

While it is a matter of common knowledge that municipal indebtedness generally increased in most cities after the war and has remained higher than preceding the war, in Washburn while this indebtedness likewise increased immediately preceding the war from Thirty Five thousand six hundred ninety two and 50/100 ($35,692.50) Dollars in 1913 to Eighty five thousand three hundred ninety three and 75/100 ($85,393.75) Dollars in 1927, after that it was decreased to Thirty Five Thousand ($35,000) Dollars by 1929 (R. 114). These conditions hardly justify any conclusions approaching those portrayed in appellants' brief.

6. The Commission under the decisions of the state and federal courts was required to give consideration to and have its valuation reflect such consideration of the increased cost of reproducing the property at present day prices.

While it appears in the record that the speculative value of the war period has been discounted by subsequent evidence, there is no evidence in the record showing or justifying any conclusion that the wiping out of the speculative value has in any manner affected the true value of this very necessary utility in the city of Washburn, nor is there any evidence showing, what, if any, effect the conditions recited by the Commission had or might have had on the values of the water works property. The Commission merely recited the existence of these conditions and then arbitrarily guessed that they must have had some effect upon the value of the water works property and therefore ignored the only competent evidence in the record as to the value of this property.

B. The valuation alleged by the Commission to reflect the cost of reproduction as of the time of its decision was in fact inadequate.

1. The valuation thus submitted by the Commission's engineers being of a date eleven months preceding the actual decision, during which time a material change in prices took place, and since the prices on the date of this decision more nearly reflected the average prices during a considerable period preceding the valuation, the valuation figures adopted were inadequate.

As indicated in the statement of facts herewith, the Commission's engineering staff took as their valuation date January 1, 1928. This date reflected prices below the normal prices existing since 1923, so far as they affected this utility property (R. 85). After this valuation eleven months were permitted to elapse before the Commission announced its decision. In the meantime the cost of reproducing the property had increased over $7,000.00 (R. 86, 97). Moreover an additional $1,000.00 of equipment had been added.

The engineering valuation approved by the Commission in its decision, omitted $2500 to $3000 of working capital and material and supplies and made no allowance for going value. A valuation as of January 1, 1929, by the Commission's engineering staff or twenty-seven days after its decision, submitted in this case, shows that the proper cost of reproduction valuation as of the date of the decision would have resulted, even on the Commission's methods in a value of $95,865.00 (R. 97) without any allowance for going value as against the $87,000.00 approved by the Commission. The higher valuation which thus resulted is confirmed by the other valuations by the Commission. (R. 7-9).

The valuations of the Commission show a studied effort to cut value wherever possible, as evidenced by the analysis submitted in the statement of facts herein. It is further demon-

strated by the analysis of depreciation in the statement of facts.

2. One reason for the low cost of reproduction valuation submitted by the Commission's engineers is the unjustifiable depreciation of the property.

This is demonstrated by a reading of the analysis in the statement of facts herewith. The appellants' counsel seeks to justify it however and in doing so misconstrues the effect of the testimony.

The record is clear that the Commission's engineer Thiesen and the plaintiffs' engineer Hartt both based their estimate of the extent of depreciation of the property on the results of an examination of the property. Hartt shows a broad experience and familiarity with the factors affecting depreciation. Thiesen who also made a valuation in 1924 seems not to have even the confidence of the Commission at the time of the 1924 decision. In that decision, however, the Commission accepted the sinking fund method of depreciating property the same as used by Hartt in his valuation in this proceeding.

Thus we have the experts agreed as to the method of determining depreciation in 1924 and pursuing like methods of determining such depreciation in 1929 but arriving at a different result primarily because the Commission had abandoned the sinking fund method of depreciating property which it had previously approved. The result is that as to the cost of reproducing the property the variation between the figures of these engineers is but 10% but after depreciation the variation is 22%. On the other hand if the same method of depreciation had been used by Thiesen in 1928 that he used in 1924 the variation between the figures after depreciation would have been 13%.

The result therefore is that after the Wisconsin Supreme Court in the *Waukesha case,* 191 Wis. 565, 569, compelled the

Commission to abandon its split inventory valuations, the Commission promptly abandoned its former approved policy for one that would help it arrive at a similar result by cutting the value of the property down on another theory, and so it adopted the straight line method of depreciation. This method is not used by the industry and does not actually reflect conditions in the industry, because the straight line method is not used by the industry and does not actually revested but is held without earning anything from the time of accumulation to the time of actual use in replacing the property.

The difference between the engineers therefore does not result from the method by which the actual deteriorated condition of the property is determined, but rather from a difference as to what should be done with the fund that is to be used to replace the property. For this reason the criticisms and authorities referred to by counsel are not in point.

C. The Commission under the decisions of the state and federal courts was required to give consideration to and have its valuation reflect such consideration of the increased cost of reproducing the property at present day prices.

The rule of the courts however is that in view of the "great advance in prices during and after the war" a valuation of public utilities property must "reflect actual value of the property as of the time the valuation is made." "A valuation which does not as to tangible property substantially reflect the then cost of reproduction less depreciation does not meet the requirements."

Waukesha Gas & Electric Co. vs. Railroad Commission, 191 Wis. 565 at 569.

Ashland Water Company vs. Railroad Commission, 7 Fed. (2nd) 924 at 929 and 930.

State ex rel. Southern Bell Telephone Co. vs. Public Service Comm., 262 U. S. 276.

Georgia Railway & Power Co. vs. Railroad Commission, 262 U. S. 625.

Bluefields Waterworks & Improvement Co. vs. Public Service Comm., 262 U. S. 679.

Ohio Utilities Co. vs. Public Utilities Comm. of Ohio, 267 U. S. 359.

Standard Oil Co. vs. Southern Pacific Co., 268 U. S. 146.

Brush Electric Co. vs. Galveston, 262 U. S. 443.

Monroe Gas Light Co. vs. Michigan Public Utilities Comm., 292 Fed. 139 at 143.

McCardle vs. Indianapolis Water Co., 272 U. S. 400.

Van Wert Gas Light Co. vs. Michigan Public Utilities Comm., 299 Fed. 670 at 673.

New York Telephone Co. vs. Prendergast, 300 Fed. 822.

Consolidated Gas Co. vs. Prendergast, 6 Fed. (2nd) 243 at 280.

Minneapolis vs. Rand, 285 Fed. 818 at 826 and 827.

Mobile Gas Co. vs. Patterson, 293 Fed. 208 at 211 and 218.

Joplin Gas Co. vs. Public Service Comm., 296 Fed. 271 and 277.

Consolidated Gas Co. vs. Newton, 267 Fed. 231 at 236-238.

In the Waukesha case, supra, it was said:

"Hence where there has been a period of rising prices for many years, original cost plus cost of additions do not correctly measure the present value. Such a method may form the main basis of a valuation during the period of fairly

stable prices, but it does not as applied to prices from 1912 and earlier down to 1922. Since the basic result to be reached is the present and near future fair value of the property, any method that will accomplish that result is a proper method. It is doubtful if any method will accomplish such result unless it *substantially* reflects or agrees with present or recent reproduction cost less depreciation. The method employed by the *Commission* in the instant case does not do so, and under the federal rule referred to must be set aside as confiscatory and unreasonable."

The method applied in the Waukesha case, supra, by the Commission was the so-called split inventory method of valuation using the average prices prior to 1916 for property installed prior to that date, and adding thereto the cost of the property after 1916 as to any such additions. In this case the commission in form considered present day prices, then rejected them, and accepted less than the depreciated split inventory valuation with materials and supplies, and working capital, but without going value.

St. Louis & O'Fallon R. Co. vs. U. S., 279 U. S. 461, 486.

The decision here as in the case above

"carefully refrains from stating that any consideration whatever was given to present or reproduction costs in estimating the value of the carriers' (plaintiffs') property."

The Commission here resorted to a method of cutting down value identical to that condemned in

Ohio Utilities Co. vs. Comm., 267 U. S. 359, 362, 363,

in that it had before it undisputed evidence of value but arbitrarily ignored that value and substituted its own guess.

In the McCardle case, supra, the United States Supreme Court said:

> "In fact, prices and values have so changed that the amount paid for land in the early years of the enterprise and the cost of plant elements constructed prior to the great rise of prices due to the war do not constitute any real indication of their value at the present time."

In the *Ashland* case, supra, decided by a three judge court in the Western District of Wisconsin, and referring to property directly across the bay from the Washburn property, now in suit, said:

> "That dominant or controlling—or, in any event, due, or substantial, reasonable, or fair—consideration *must* be given to the evidence of reproduction costs at the time of hearing. Whatever debate may be indulged in respecting the adjective to be imported into the rule deducible from the decisions, it seems difficult to escape the conclusion reached in the *Monroe Gas* case (D.C.) 292 F. 139, that *dominant* consideration must be given; that such is the 'necessary implication' found in the *results* in those cases."

In this case the Commission employed the same method condemned by our own Supreme Court in the *Waukesha Gas* case, supra.

In this connection we submit that it conclusively appears on the record that while the Commission stated that it was giving consideration to the present cost of reproducing the property, it later used and applied the split inventory method condemned in the *Ashland* case, supra. This for the reason that the valuation ultimately allowed for rate making purposes exceeded by less than Thirty Five Hundred ($3500.00) Dollars, the split inventory valuation of this property, as determined by the Commission (Exhibit C, R. 39), and if to the split inventory valuation we add allowance for working capi-

tal, materials and supplies and subsequent additions, the value arrived at is less than the depreciated split inventory value.

That being true this case was clearly decided in deliberate disregard of the Court's decision in the *Ashland* case, supra.

D. By not allowing going value and failing to fix that element of value in this case the Commission deprives the plaintiffs of an element of value and therefore of a property right.

All of the estimates of value prepared by the engineering staff of the Railroad Commission specifically stated that they did not include any allowance for going value, materials and supplies on hand or working capital. This was an important element in the decision in this case, and under the decisions the plaintiff was entitled to a determination of the going value, material and supplies on hand and working capital, and to the inclusion of these elements of value in the order made by the Railroad Commission.

Southwestern Bell Telephone Co. vs. City of Ft. Smith, 294 Fed. 102, at 103 and 106. (Affirmed by the United States Supreme Court on the authority of previous cases. See 70 L. Ed. 236, memorandum decision).

Mobile Gas Co. vs. Patterson, 293 Fed. 208 at 216.

Minneapolis vs. Rand, 285 Fed. 818, 830.

Public Service Railway Co. vs. Board of Public Utility Commissioners, 276 Fed. 979 at 987.

Ohio Utilities Co. vs. Comm., 267 U. S. 359, 362, 363.

E. The plaintiffs are entitled to the "independent judgment of the court as to both the law and the fact" especially where it is apparent from the proceedings that a deliberate attempt on the part of the Commission is being made to circumvent the decisions of this court guaranteeing due process.

As shown in the statement of facts the Commission's engineers have depreciated the property of this company way below their previous conclusions. The Commission after waiting nearly a year before rendering its decision accepted without readjustment the cost of reproducing the property at a figure over $7,000.00 less than actual cost. This, as indicated above was due to the fact that at the time the Commission's engineers made their valuation there was a temporary slump in prices which recovered during 1928. This fact the Commission, however, wholly ignored, though it was evident by December 4, 1928, the date of its decision (Hartt Aff. R. 85).

It absolutely ignored items for going value, materials and supplies and working capital unless it can be said that it accepted the split inventory valuation and added these items, except going value, to that valuation to arrive at the $75,000 decision.

The admitted action of the Commission in proceeding to cut actual operating expenses over $5,000 annually, without evidence in the record to support such action, should cast suspicion upon the whole result of the Commission's action. (R. 10-11, 14, 57, 60, 61).

The determination of the Commission as late as 1925 that the revenues were inadequate to earn a fair return on even $53,000 of value (R. 7, 12, 13) should require careful scrutiny of its later determination especially since operating expenses and revenues remained stationary.

The change in the method of determining depreciation of the property, resulting in the great disparity in comparison

of condition of the property between 1924 and 1928 is also evidenced by arbitrariness challenging attention. (R. 86, 87). (See infra, analysis statement of facts.)

Under these circumstances this court should judge for itself what the facts are.

Ohio Valley Water Co. vs. Ben Avon, 253 U. S. 287, 289.
Bluefield Co. vs. Public Service Comm., 262 U. S. 679.

In the latter case the court said:

"Plaintiff in error is entitled under the due process clause of the Fourteenth Amendment to the independent judgment of the court as to both law and facts. *Ohio Valley Water Co. vs. Ben Avon Borough,* 253 U. S. 287, 289, and cases cited." (262 U. S. 689).

F. The Commission's only justification for ignoring the decisions of the courts are the conditions referred to above but the record fails to disclose any justification for such action and nowhere in the evidence is it shown that the conditions relied upon by the Commission had any effect upon the value of the property of the plaintiffs.

Notwithstanding the fact that its decision of 1924, fixing a value of Fifty Thousand ($50,000.00) Dollars for this property (Exhibit A) had been set aside by the Circuit Court of Dane County, as being inadequate and purely arbitrary and in violation of the decisions of the Federal Court as well as the Supreme Court of the State of Wisconsin, the Commission in its decision and order (Exhibit C, R. 39) reiterated part of its language condemned by the court in the previous decision.

The conditions referred to by the Commission in the 1924 order, which has been set aside as illegal, and from which

decision the Commission has not seen fit to appeal, recited the fact that the abnormal growth of Washburn during the war was checked and reaction set in after the war, resulting in the removal from Washburn of a considerable number of people. Using this testimony as a basis and without determining the value of the property in Washburn during the war, the Commission proceeds to reduce the value of the Washburn Water Works property below cost and at the arbitrary figure of Seventy Five Thousand ($75,000.00) Dollars. In other words it took one type of Washburn property and increased its value during the war several fold then it took the Washburn Water Works property, never increased its value correspondingly, but assumed that it decreased in value, not from the high level of war time but from the lower level of actual cost. This method the Circuit Court of Dane County declared to be arbitrary, but notwithstanding such declaration, the Commission readopted it in the present case. In so doing the Commission was arbitrary and unfair to the plaintiffs.

Ashland Water Co. vs. Railroad Commission, 7 Fed. (2nd) 924 at 935 and 936.

Wisconsin-Minnesota Light & Power Co. vs. Railroad Comm., 183 Wis. 96 at 103 and 104.

In the Ashland Water Company case, supra, page 935 the court said:

"But the suggestion that apprehension growing out of a decrease of population is sufficient to justify a court in utterly ignoring a rule requiring *due* or *reasonable* consideration to be given to evidence of reproduction cost challenges attention, when once we consider its effect upon judicial duty. Plainly, it suggests that commissions and courts may broadly divide communities having utilities into at least three classes: Those which are 'live' and 'pro-

gressive'; those which are 'stable' or 'standard'; those which are 'stagnant' or 'retrogressive' in respect of population. And if this phase is of the importance sought to be given it in this case, of course it must lead to a discharge of duty both with respect to values, and to utility rates which afford return upon 'fair' values (in a constitutional sense), which will square with that fundamental idea. The circumstance of progressive increase of population of *itself* must entitle a utility in a rich and progressive community to relatively higher rates, the second class will be entitled to receive only a sort of 'standard' rate or consideration, while the utility in a stagnant community, no matter what the cost of its property, must bow to a retrogressive rate—that is, 'relatively' retrogressive.

It would seem to approach the ludicrous to put these considerations forward as a basis for ignoring wholly reproduction cost evidence, and yet, at the same time, allow a commission or a court to consider seriously property in a stagnant community on the basis of *reasonably prudent investment value*. It amounts in substance to this: That not only with respect to reproduction cost evidence, but with respect to evidence bearing pertinently upon any other rule or theory of value, commissions and courts are always endowed with a power, if the community may be characterized loosely as stagnant or retrogressive, to decree that the utility entitled to have its property valued shall have *dying* values and *dying* rates. It suffices to note that the commission never saw fit to develop the case along this line, and, if it had, the views above sought to be elaborated are equally tenable against any possible plan or scheme of valuation, and, of course, destroy the rule which the plaintiff here can invoke, namely, that *reasonable consideration* must be given to reproduction cost evidence."

Bearing in mind that the observations of the court in the latter case apply to a situation immediately across the bay from Washburn, it is of course to be observed that such a method cannot be right in one place and wrong in the other,

and that this procedure must condemn the proceedings of the Railroad Commission.

It may not be amiss to say that following the decision of this court in the Ashland water case, a new application was made to the Railroad Commission for an increase in rates in that city, and after the testimony was closed the Commission could find no escape from increasing the rates above those fixed by the order of this court unless the city would agree to waive the increase in taxes because of the higher valuation fixed by this court. As a result of this recommendation the city did waive the increased taxes and the case was settled on that basis. All of this appears from the records of the Railroad Commission, of which this court will take judicial notice.

G. The efforts on the part of the Commission to find a value by comparing rates in Washburn with rates in other communities and the claim that the rates in Washburn were unusually high and that this fact affected the value of the property were clearly erroneous.

As one of its reasons for allowing a low valuation for the property of this company, the Commission in its order of 1924 (R. 30) discussed the question of rates in Washburn and attempted to compare these rates with rates in other communities. The only evidence in the record as to comparative rates related to other cities of the state wherein the waterworks properties were owned by the municipalities, and where by reason of not taxing such utilities, and by reason of managing the properties through salaried officials of the city whose salaries are not allocated or apportioned to the utilities, these municipalities are able to operate their plants with less expense actually charged against them than could pri-

vate concerns. That fact of itself discredits the effort of the Commission in this regard.

Ashland Water Company vs. Railroad Comm., 7 Fed. (2nd) 924 at 937.

"Each utility in each community is entitled to a valuation upon evidence legally pertinent to its property; not merely, in difficult cases, to a referendum to other cities. There can be no need of rules or principles guiding commissions in valuations of property, if such considerations may dominate *evidence* of value in the particular case."

THE COMMISSION HAS IGNORED ACTUAL OPERATING EXPENSES AND SUBSTITUTED ITS OWN ESTIMATE OF WHAT SHOULD BE PROPER OPERATING EXPENSES, THEREBY DECREASING THE ALLOWANCE FOR EXPENSES OF THE COMPANY BY OVER $5,000 WITHOUT ANY EVIDENCE TO SUPPORT SUCH ACTION.

A. The reduction of actual pumping costs by $1,650 annually was arbitrary.

The complaint alleges that

"In order to arrive at the arbitrary and unreasonable estimate of operating expenses used by the Commission in arriving at its decision of December 4, 1928, the Commission stated as reason for not accepting the actual expenses as above set forth, was, that in their judgment pumping expenses were too high.

"To reduce this item they recommended the installation of an additional smaller electric pump, which would necessarily be required to operate longer hours, would improve the electric load factor and thereby reduce the rates that would be charged for the electric energy consumed. At the

time of the hearing, however, the experts, representing the Commission, stated that they had insufficient proof to warrant such a conclusion, and nowhere in the records is [fol. 20] there any proof supporting the ultimate conclusions of the Commission and the recommendations of the Commission are absolutely refuted by the undisputed testimony in the record." (R. 14).

This charge in the complaint is admitted in the following language of the answer:

"Defendants admit that the railroad commission discounted and reduced the actual operating expenses of the company by determining that it should install an additional electric pump. * * Defendants admit that the Commission arrived at an estimated net saving in pumping costs of $1,650.83, thus reducing pumping costs from $6,558.83, as shown by the annual report of 1927, to an estimated figure of $4,908.00." (R. 57).

And also stated

"Defendants admit that the commission recommended the installation of a smaller electric pump, which would be required to operate longer hours, which would improve the electric load factor and thereby reduce the rates charged for electric energy consumed. *Defendants admit that at the time of the hearing the experts representing the commission stated that they had insufficient proof to warrant such conclusion.* Defendants allege that subsequent to said hearing, evidence was secured to show that the pumping cost could be reduced in accordance with the estimate of the commission." (R. 60-61).

So that at some time after the hearing before the Commission, without notice to the plaintiffs, the engineers of the Commission came to a conclusion which they could not justify under oath at the hearing before the Commission.

In this connection, however, it is interesting to note what these conclusions of the engineers representing the Commission actually were, as reflected by the same conclusions submitted in this case. It is said:

"It is not proposed to dispense with the large centrifugal pump for it is needed at times when the reservoir has an insufficient supply of water for fires. In order to secure the lower rate for power the large motor and pump must be idle and with *intelligent operation* and *fortunate distribution of large fires or other necessity* of operating the large pump a substantial saving may be made. The margin appears to be sufficient to write off the fixed charges and the cost of additional equipment and labor of installation within a few years assuming occasional use of the large pump and motor now installed with *wise handling, proper installation* and *cooperation*, and *favorable circumstances*, the saving *may* amount to two thousand dollars a year." (R. 105-106).

The Commission apparently adopted the qualified conclusions of its engineering staff as is evidenced by the following statement in its order of December 4, 1928:

"It is not proposed to dispense with the large centrifugal pump for it is needed at times when the reservoir has an insufficient supply of water for fires. In order to secure the lower rate for power the large motor and pump must be idle and with *intelligent operation* and *fortunate distribution of large fires or other necessity of operating the large pump* a substantial saving may be made. The margin appears to be sufficient to write off the fixed charges and the cost of additional equipment and labor of installation within a few years assuming occasional use of the large pump and motor now installed. With *wise handling, proper installation* and *cooperation*, and *favorable circumstances*, the saving *may* amount to two thousand dollars a year. * * (R. 39, 40).

That then constitutes the basis for ignoring actual operating conditions and actual operating expenses, and, is advanced as the justification for submitting the Commission's estimate of pumping expenses for the company's actual history showing operating expenses. By this means the Commission cut the actual pumping expenses from $6,558.83 for 1927 to $4,908.00. (R. 10, 57).

The plaintiffs on the other hand show that in complying with the Commission's suggestion in its order of 1925, wherein the Commission estimated the annual saving of $3,000 in pumping costs if an electric pump were installed, as against the steam pump operation (R. 15, 61) installed an electric pump with the result that pumping costs in 1925, the last full year of steam operation, were $7,923.06 (R. 33) against $6,558.83 in 1927, the first full year of electrical operation (R. 10, 57) or a reduction of less than $1400. This reduction was actually less than the difference between the cost of steam plant operation in 1925 over 1924 (R. 33).

The care with which the present installation of the electric pump was made is evidenced by the affidavit of Mr. Maxcy, the manager and receiver of the water works company when he says

"Affiant further says that with respect to the pumping costs criticized by said Railroad Commission that prior to the installation of the present pump, affiant made a careful investigation to determine the proper size of such installation and consulted with T. W. Gray, an experienced water works builder and operator with over thirty years experience, and also had information from the engineers of Allis-Chalmers Company, and as a result of such investigation and the advice received from such sources, this affiant made the installation of the type and size of pump now criticized by the Railroad Commission; that considering all of the demands of the City of Washburn, it is the opinion of this affiant and was the opinion of such experts

that a pump of the size now installed was necessary; moreover in making such installation, consideration was also given to the fact that in the event of a failure of the reservoir at any time, resort must be had to the pump for direct pressure in the event of an emergency such as a fire, and to meet such an emergency a pump of the size installed was and is absolutely necessary.

Said pump having been installed in reliance upon the opinion of such experts, affiant thereupon proceeded to enter into a contract with the Lake Superior District Power Company, which commits him to a minimum annual bill in excess of the estimate for electric energy referred to in the Commission's order of December 4, 1928; and said contract will not expire until May 1, 1931; said contract being made in the light of the particular installation of the particular pump criticized by the Railroad Commission." (R. 79).

Moreover, as appears from the affidavit above, the plaintiffs are now bound by contract until May, 1931, to buy on the basis of the present rates and could not obtain the reduction hoped for by the Commission, if they tried. Here again the action of the Commission is purely arbitrary and unjustified.

The decrease in the recorded pumpage is not due to the increase in metered customers and therefore does not sustain the Commission's attempt to criticize operating expenses on the account of refusal to install more meters.

A marked variation is shown in the pumpage of this plant:

"Year	Pumpage during the year, gallons
1928	59,340,000
1927	68,550.000
1926	97,311,264
1925	135,961,411
1924	146,051,576
1923	155,815,111
1922	169,264,142
1921	171,682,162
1920	164,282,880"

(R. 103).

Following the tabulation of this result in its order of December 4, 1928 (R. 40) the Commission says:

"A considerable part of the excessive pumpage year after year can be attributed to no other cause than the lack of restraint on customers as regards the waste of water. By January 1, 1923, only 51 meters were in use. During 1925 21 additional were installed, while in 1926 40 more were placed. During 1927, 44 meters were set, making a total of 156 metered and 369 unmetered customers on December 31, 1927. We believe the decrease in pumpage noted above is due largely to the installation of meters." (R. 40, 41).

The plaintiffs deny this and explain the decrease in pumpage as follows:

"The steam pumps, referred to above, were depreciated 75 per cent by this affiant in making his valuation (see valuation detail, page 13) largely because of evidence of excessive slippage developed by such pumps. The pumpage computed by the company is not measured by accurate meters, but is measured by counting the strokes of the steam pump and by determining the length of time the electric pump operates. The pumpage computed during the time

the steam pump was in operation was considerably in error, due to the excessive slippage, while the electric pump is new and computing pumpage from hours and minutes of operation gives a more accurate estimate of the amount of water pumped. This, in my judgment, accounts for the greater part of the difference in the pumpage in 1926 and 1927. The fact that 1926 had seven months of steam pumpage and five months of electric pumpage emphasizes this conclusion when compared with the figures of 1927." (R. 87).

W. G. Maxcy, with thirty years of experience as an owner and operator of twelve or more utilities (R. 45) stated that as manager of the property of the plaintiffs he has studied the meter situation and in his judgment the additional cost incident to the installation of meters, maintenance thereof, reading and billing would more than offset operating expenses resulting from greater pumpage, due to waste of water by unmetered customers. (R. 77).

Defendants plead

"—that they have no information sufficient to form a belief as to the truth of the allegations contained in paragraph XVII of said bill of complaint to the effect that by reason of the nature of the business and the additional operating expenses incident to the reading of meters, repairing of meters, change or installation of meters, as well as other similar expense and the carrying cost of such property, it is not economical to install more meters, and that the saving incident to the use of meters is less than the sum of such items of expense." (R. 62).

Nowhere in the record are the claims of the plaintiffs contradicted. All that the Commission's engineers say is that meters reduce water consumption (R. 104). This is all therefore that persuaded the Commission to set its judgment against that of the management of this company.

B. The reduction of distribution, commercial and general expenses below the actual previous amounts for such items was purely arbitrary.

The complaint alleges that these items were reduced without any evidence in the record justifying such action. (R. 10, 11).

The answer admits this charge by saying "Defendants admit that the distribution, commercial and general expense was cut by the order of the Commission in the amount of $2,718.45," but it denies that such conclusion was not supported by the record before the Commission.

At the hearing in the lower court no evidence was offered to sustain or justify any of these reductions nor was there any evidence offered showing why the Commission made these reductions. All of the evidence offered by the defendants was directed to the proposition that the pumping costs could be reduced by the installation of a smaller pump. For this reason the action of the Commission must be supported, if at all, upon the proposition advanced by the Commission in its decision that "from our knowledge of prevailing financial conditions of business enterprises in Washburn, it is apparent that the water utility is in a much better financial condition than other classes of business" and undoubtedly the Commission concluded that under those circumstances the water utility would simply be denied part of the necessary operating expenses for the items referred to. This action of course again was purely arbitrary.

C. The failure to allow amortization of accumulated legal expense and receiver's fees was wholly arbitrary.

This, then, is the basis upon which the Commission cut the pumping expenses by $1650.00 and the distribution, commer-

cial and general expenses by $2718.45 (R. 57). Moreover it refused to consider management and legal expenses accrued in "fighting this Commission's orders," although the answer admits this "fighting" was always successful and also that not all of the expenses included were for this purpose (R. 58), the expenses representing an effort to obtain adequate rates as well as to prevent confiscation of the plaintiffs' property under the purchase proceeding set out in the record (R. 21-31). The accrued expenses amount to $5,000 and should be amortized over a five year period.

D. By thus substituting a theory of operating expenses over $5,000 less than the actual operating expenses the Commission improperly and illegally interfered with the management of the company and the result thus obtained can therefore not be sustained.

In thus disregarding actual experience of the plaintiffs the Commission had no evidence to support this practice and further it set its judgment of what were proper operating expenses against the actual history and the judgment of those in charge of the property, and in these respects the Commission violated the rules laid down by the Federal and Wisconsin courts.

Without any foundation in the record and contrary to the experience and judgment of the plaintiffs, the Commission thereafter set its judgment against the experience and judgment of the plaintiffs. The arbitrariness of this action is further evidenced by the fact that in two previous decisions, the Commission had found that the plaintiffs' rates were inadequate and did not provide an adequate return on a valuation of about $53,000 (R. 12, 13, 59).

State ex rel. S. W. Bell Telephone Company vs. Public Service Commission, 262 U. S. 276, 288, 289 (1923).

S. W. Bell Telephone Company vs. Fort Smith, 294 Fed. 102, 198 (W. D. Ark. 1923). Affirmed 70 L. Ed. 236.

St. Joseph R. L. H. & P. vs. Public Service Commission, 268 Fed. 267, 268 (W. D. Mo. 1920).

Minneapolis, St. P. & Ste. M. R. R. vs. Railroad Commission, 136 Wis. 146, 164.

Wisconsin-Minnesota Light & Power Co. vs. Railroad Commission, 183 Wis. 96.

Wisconsin-Minnesota Light & Power Co. vs. Railroad Commission, 183 Wis. 104, 105.

Ohio Utilities Co. vs. Comm., 267 U. S. 359, 362, 363.

"The Commission arrived at its conclusion by substituting for the experience of the company estimates as to future revenues and future operating costs. In setting aside the existing rate the Commission cannot substitute for the experience of the company its estimates as to the future revenues and operating costs. * * Estimates as to revenues could not change the fact as it existed." (*Wisconsin-Minnesota Light & Power Co. vs. Railroad Commission,* 183 Wis. 105, 106.)

The exclusion of the legal expenses of the company was improper because this was an element of expense incident to the operation of this company which the public is required to bear.

Monroe Gas Light & Fuel Co. vs. Michigan Public Utilities Commission, 11 Fed. (2nd) 319-325.

Winona W. M. L. & P. Co., 276 Fed. 996.

Patterson vs. Mobile Gas Company, 293 Fed. 208.

Columbus Gas & Fuel Company vs. Columbus, 17 Fed. (2nd) 630 at 640.

Spring Valley Water Works vs. San Francisco, 192 Fed. 137, 190.

San Diego Water Works Co. vs. San Diego, 50 Pac. 633; 118 Cal. 556, 574.

UPON EITHER OBJECTION RAISED BY THE RECORD THE ORDER OF THE COMMISSION MUST FALL.

From what appears by the admissions of the defendants in this case the order of the Commission cannot stand. If the court were to disregard the arbitrariness of the finding of value entirely it is clear that even on the value found and with the past experience of the plaintiffs, the revenue provided by the Commission was less than the actual operating expenses, taxes and depreciation, and that nothing has been provided for return. On that basis, on the Commission's own valuation and its finding of seven per cent return as being reasonable, a proposition which we are not ready to concede, additional revenue of $5,250 is required to avoid confiscation.

The decree in this case does not fix a rate base, it finds no value, it merely sets aside the order of the Commission and enjoins any steps to enforce the order of the Commission dated December 4, 1928, and further enjoins interference with rates providing adequate returns, and from intrefering with the plaintiffs in charging adequate and reasonable rates, rendering a fair and adequate return on the value of the property of the plaintiffs used and useful in its business.

It leaves the Commission free to reconsider the rates of the plaintiffs and admonishes it only to respect the laws of the land.

For these reasons the decree should be affirmed.

Respectfully submitted,

H. L. BUTLER,
H. H. THOMAS,
B. H. STEBBINS,
R. M. STROUD,
R. M. RIESER,

Attorneys for Plaintiffs and Respondents.

OLIN AND BUTLER,
Of Counsel.